# DOW THEORY LETTERS INC.

RICHARD RUSSELL
P.O. Box 15428
San Diego, Calif. 92115

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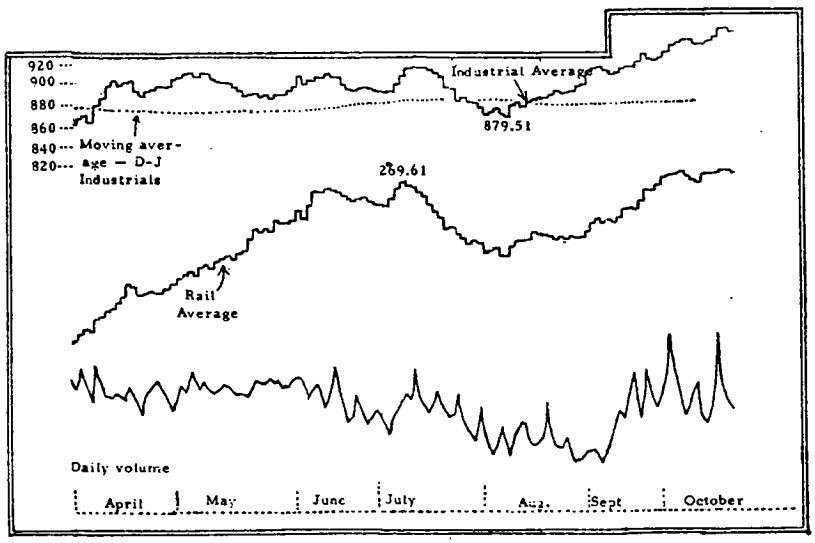
THE MARKET: It is probable that the market last week discounted the best of many happy possibilities. At the year's high of 967.49 (October 18), the Dow was discounting the possibility of a Vietnam peace, the strong probability that Nixon would be elected President, and the chances that business would remain strong and that inflation would continue.

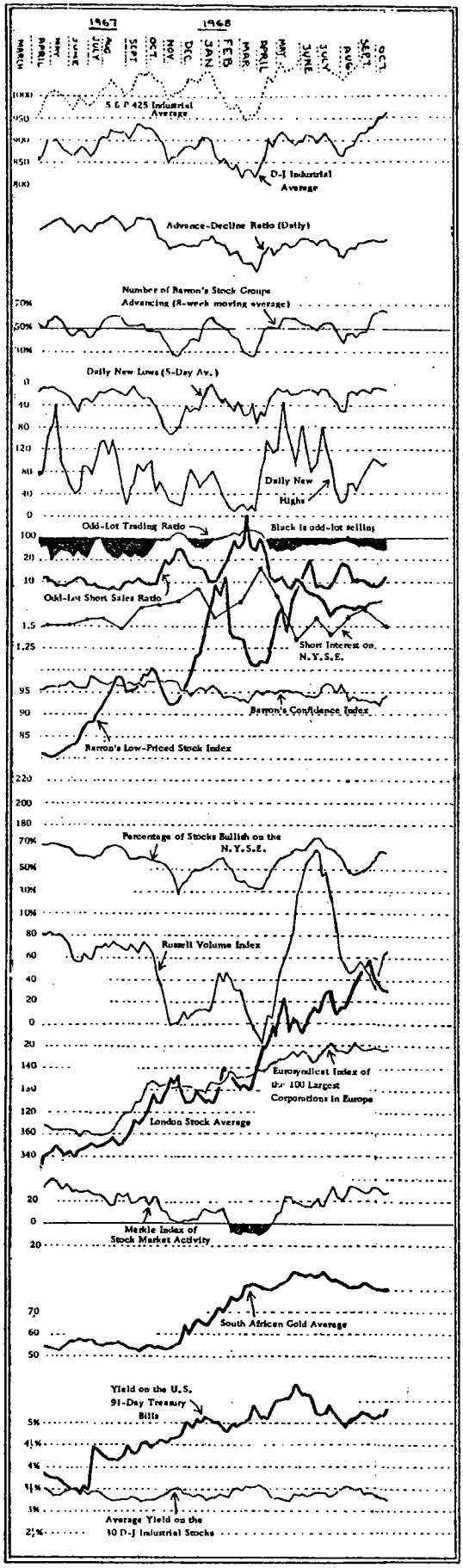
The Rails too were playing out an interesting drama, having come within points of their 1967 all-time high of 274.49. Yet despite an abundance of volume and speculative activity, the carriers displayed a curious reluctance to move the final few points which would take them above the 1967 peak.

It is well to note that the Dow has unleashed a long and top-heavy list of advances since the August 15, 1968 low of 879.51. Of the 45 trading days since August 15, the Dow has advanced on 36 occasions. Robert Rhea discovered long ago that during both bull and bear markets the Dow advances about as often as it declines. Thus, I feel that we are now probably very near the "evening up" process, and that the Dow is now near a declining phase.

A second consideration is that my five-day average of daily new highs has not confirmed the strength in the Dow. Thus, from the 220 (five-day average) peak in new highs set last June, the new high index declined, then rose to a peak of 160 new highs recorded in July. A second decline in the new high index occurred, and on the recent (August to October) market rally, the new high index reached a peak of only 125 (on October 3). This provides a picture of descending peaks in the new high index, 220, 160, 125. I consider this phenomenon a negative influence on the market and one that bespeaks of "lack of strength."

A third consideration (as discussed last week) is the July to October cave-in on Barron's Confidence Index. This decline calls for a top in the Dow during the September-November period with accompanying weakness carrying to the end of the year. The Confidence Index should not be used



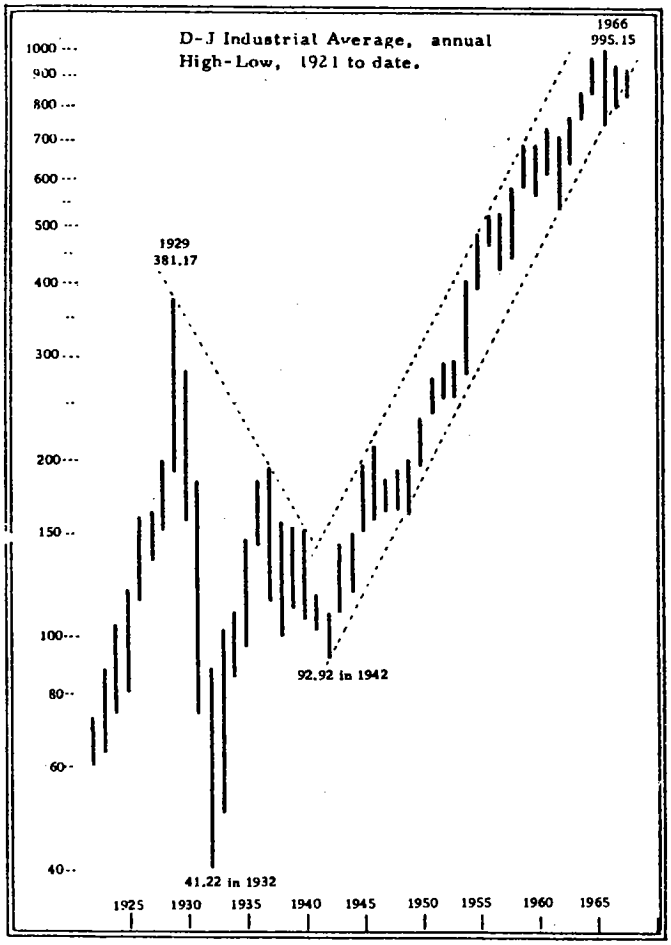


1967
1968
S & P 425 Industrial Average
D-J Industrial Average
Advance-Decline Ratio (Daily)
Number of Barron's Stock Groups Advancing (8-week moving average)
Daily New Lows (5-Day Av.)
Daily New Highs
Odd-Lot Trading Ratio
Odd-lot Short Sales Ratio
Short Interest on N.Y.S.E.
Barron's Confidence Index
Barron's Low-Priced Stock Index
Percentage of Stocks Bullish on the N.Y.S.E.
Russell Volume Index
Eurosyndicat Index of the 100 Largest Corporations in Europe
London Stock Average
Merkle Index of Stock Market Activity
South African Gold Average
Yield on the U.S. 91-Day Treasury Bills
Average Yield on the 10 D-J Industrial Stocks

 as a barometer of amplitude, but it does have a good historical record for calling reversals of trend (direction rather than amplitude).

But the most important consideration in today's market is the direction of the primary trend, which has remained highly deceptive but bearish. It has been 32 months since the Dow recorded its 1966 bull market peak of 995.15. Since 1966 the Industrial Average has received every conceivable form of stimulant from a flooding of the U.S. money supply to planned inflation and low unemployment, peace rumors, record Gross National Product, mass mergers, record volume, and frenzied speculation on Wall Street. Yet the Industrials have yet to better their 995.15 high, and one wonders what would have to happen in order to propel them over the 1966 peak.

The funds, the institutions and the public are now in the market as they have never been in before. Everything which has not been "nailed down" has gone public, new funds are announced almost weekly, corporate mergers are the order of the day, conglomerates have been assembled, the Street has received an acceptance and aura of glamor unparalleled in market history. Daily transactions during 1968 are approximately twelve times that of 1949. Never have so many people been in a position to be hurt by an error in foresight. That's the time when errors occur on Wall Street. "Bear markets," as I have said before, "are made to part people from their money."

NO LOOKING DOWN: In Letter 405 I wrote a piece in which I stated that the U.S. Treasury and the U.S. population had "a fantastically vested interest in prosperity." Because of mountainous current debts and the need for servicing those debts, "No politician can take a chance on cooling off the boom, the Federal Reserve Board dare not slow the boom, there is no one who dare take his eyes off the top of the mountain and look down."




In a subtle way, the Dow Jones Industrial Average is reflecting the same situation. The accompanying chart shows the annual high and low for the Dow for the years 1922 to the present. The outstanding thing about this chart (at least from our standpoint, today) is the 27-year rising channel. This is a channel which started at 92.92 in 1942 and has held to the present.

Note, however, that the bottom of the channel comes at about 900 for the year 1968. Thus for a good portion of this year, the Dow held under the lower limit of the channel. For 1969, the lower limit of the channel will rise to approximately 950.

This presents an interesting situation. Presently, the Dow is above 950, and if it remains at 950 or above during 1969 there is no question but that the great rising channel will continue intact.

However, any potential decline between now and early 1969 will put the Dow below the rising channel. Since 1942 no full year of Dow action has produced a high-low bar below the channel. The question is, will 1969 produce the first exception?

As a general rule in stock market history, the longer a trend the more valid the trend. In my opinion, the rising channel of the Dow since 1942 is the most important trend in the world financial situation today. I believe that any true shattering of the trend since 1942 will hold the most serious implications for the U.S. and world stock exchanges. To put it another way, after 27 years of ascending high-low trends in the Dow, a reversal could suggest disastrous consequences.

That is why I titled this section "No Looking Down." One almost senses, as he studies this chart, that the Dow (like the economy) "cannot afford to come down off the mountain top."

It is notable that although the 1921-29 rising channel was steeper than the 1942-to date channel, the current channel has lasted over three times as long as 1921-29. During the aftermath of 1929, it was the U.S. population which ran into severe financial straits. The Government remained solvent, the national debt being only $16 billion in 1929 (with a 1929 U.S. population of 125 million). Now with a population of over 200 million, the national debt is well over $300 billion.

I am afraid the phenomenon which is going to send the market to vastly lower depths than anybody envisions when the current channel is shattered is a collapse in both the private and the public sector of the market. Each major bear market has its post-rationale. For instance, in 1907 it was a collapse in business, in 1929 it was a speculative cave-in, in 1937 the commodity market fell apart, in 1946 the expectation of "the great Post-War depression" which downed the market. I would guess that the coming trouble will stem from Government insolvency, and a general monetary collapse.

POLITICS—1969: With the picking of Curtis LeMay as his Vice President, the Wallace popularity boom has peaked. LeMay announced that he considered nuclear weapons as just another part of the American arsenal, and that if needed they should be employed against Hanoi. This type of thinking immediately cast doubt on Wallace's judgment about picking cohorts, and the Wallace boom consequently peaked. Furthermore, nationally televised interviews with politicians in Alabama have provided America with some insights into the power-aspirations of Wallace. In Alabama, ran the typical interview, running against Wallace is tantamount to being run out of town on a bed of tar and feathers. "If you liked Hitler," said a sign at last week's appearance of Wallace in San Diego, "you'll love Wallace." The potential truth in this type of accusation is undoubtedly hurting Wallace.

Mr. Humphrey must evidently pin all his hopes on a sort of "1948 upset" with a last minute switch of votes from Nixon and Wallace to himself. What could bring off such a phenomenon. A settlement of the Vietnam war could possibility do it. Or a hideous "blooper" on the part of Mr. Nixon. Mr. Nixon, well aware of such a possibility, is being very careful to say nothing of value. I would guess that Nixon would be happy to somehow disappear between now and election time, but of course that is impossible. Therefore, he is doing the next best thing. He is saying nothing quotable, nothing notable, nothing people can be wildly for or against. And who can blame him.

So, the onus for pulling a rabbit out of the hat falls to Vice President Humphrey. And Humphrey is trying everything within reason. He is trying to arouse American sympathy by appearing the part of the fighting, honest, unloved underdog. He is challanging Nixon to debates. He is taking chances. And he is fervently hoping somehow to get President Johnson's tarnished image off his back.

The one hope, as I see it, would be a Vietnam settlement, something which would make the American voter say, "Well, the war wasn't so bad after all. And they did settle it, didn't they? And prosperity is still here, isn't it?"

Hanoi is obviously counting on a Nixon victory. Consequently, they must decide on whether they will get a better deal with a desperate Johnson Administration or a new Nixon Administration. Logic would seem to favor the former for Hanoi, but North Vietnam has been fighting this war for a long, long time, and they are not about to give it away. They know that LBJ is against the wall, and they will bluff and "play it cool" for all they are worth.

Unfortunately for Humphrey, he is saddled with his pro-war position if the war continues. If the war is settled, Johnson will receive the credit. Humphrey looks weak, his record with Johnson has been weak, he is hated by half of America which is under 25 years of age. Humphrey has failed to represent youth or protest, he has failed to represent the Establishment (at least as well as Nixon does), he has failed to inspire labor. Therefore, I would say that as far as I am concerned, I am acting as if Nixon will be elected.

What will this mean? For one thing, I believe it is going to mean a definite slowing down in inflation. It will mean a huge gap between the half of America which is under 25 and the Administration. It will mean a movement towards orthodox economics.

For instance, Alden Wells in a report received today, states: "The Nixon organization has asked us to prepare an analysis of the condition of the economy together with recommendations designed to correct possible distortions. To the extent that this report is accepted, considerable changes in our banking and money system would occur." That, I might add, is putting it mildly. Mr. Wells, an extremely knowledgeable financial analyst, will undoubtedly advocate a move to fiscal sanity and perhaps a rise in the price of gold. But the mere fact that the Nixon organization has asked

 information from such an excellent source as Mr. Wells bodes for real change in fiscal policy should Mr. Nixon be elected.

The crux of the problem, as I see it, is this: as I have written (and I have been widely quoted on this) the U.S. has a fantastic vested position in boom and inflation.

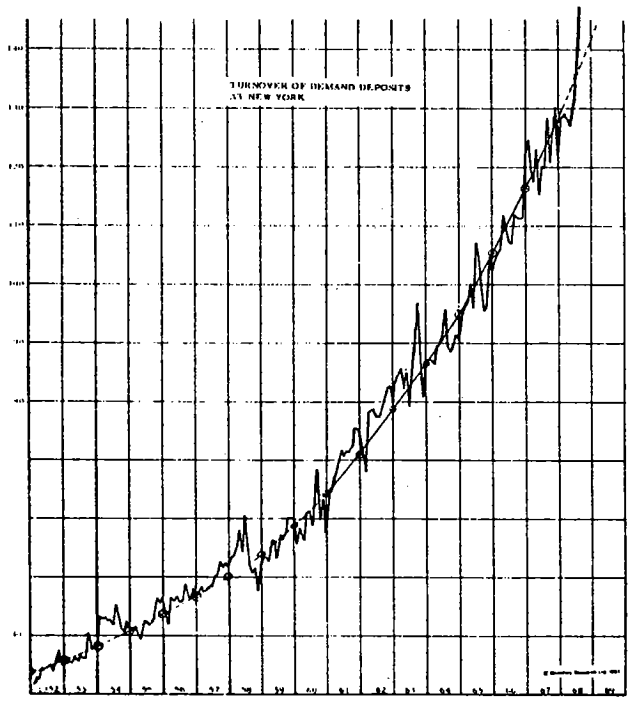
The U.S. public and private debt now stands at $1.4 trillion, having doubled in the last decade. Over the same decade the nation went further into debt by an average of $68 billion a year. Gross national product rose only half as fast during this ten years, but here is the threat. The cost of carrying this expanding debt has jumped 2½ times over the decade.

This means that the U.S. has a frenzied need for current income in order to service their debt and expenses. Boom and inflation is a built-in "must" in this kind of financial Russian Roulette. Or as the Babson's Report put it this week, "Just a bit too much deflation medicine could start our huge debt mansion tumbling about our ears."

So much for the danger of an economic slowdown and deflation. How about more inflation? These figures should prove interesting, particularly to our foreign creditors who are holding dollars (while perspiring).

| Year | Purchasing power of $ (1940 equals 100) | Year | Purchasing power of $ |
|---|---|---|---|
| 1940 | 100.0 | 1960 | 47.3 |
| 1945 | 77.8 | 1965 | 44.4 |
| 1950 | 58.2 | 1967 | 42.0 |
| 1955 | 52.3 | 1968 (Jan.) | 41.2 |
| | | 1968 (Aug.) | 40.0 |

WHITE HEAT: One feels the franticness everywhere. Two 21 million share trading days on the N.Y.S.E. within 9 trading days. demand-deposit turnover pushing towards the historic 156 velocity turnover of 1929, brokerage offices providing standing room only, individual stocks rocketing 10% in a day, Dow quotes on the radio every half hour all day long.




I continue to be fascinated by the accompanying chart (from Bolton Tremblay Bank Credit Analyst) showing the sheer velocity of turnover of demand deposits or checking activity in New York, the world's greatest financial center. The last two record-breaking months of increasing velocity of money turnover has pushed this indicator into an almost vertical position. At the latest figure of 147, demand deposits in New York are turning over at a rate of roughly three times per week. This frenzied activity is being reflected in the scattered days of huge volume on the N.Y.S.E. It is being reflected in massive institutional turnover of funds for speculative purposes, and it is now estimated that institutions account for half the volume on the Big Board.

One reads of new young financial "gunslingers" in the newspapers, a 29 year-old "empire builder" out of Denver is the man to watch, a 27 year-old Westerner who is starting a new mutual fund. One reads that the average age of the fund managers at Yale is below 40. The old fuddy-duddies of 45 and over are rendered financially impotent by the new breed of swingers. They move over and let the fearless ones wheel and deal. It is "costly" to think in terms of conservatism and safety these days. Wall Street is on fire, and the old timers are merely capable of dampening the flames.

In the history of mankind, no boom has ever been sustained. In all history, the bigger the edifice of speculation the greater the ultimate collapse when the edifice comes tumbling down. But the crowd is not thinking in terms of a tumble

or a collapse here. If and when Wall Street shudders there will be ample time to lighten up, there will be rallies, there will be orderly retreats.

I am more and more of the opinion that when this market structure comes down, the retreat is going to be one of the most disorderly in history. It would not surprise me, in fact, to see a time when the Dow drops 30 to 50 points in a single day. The volume on the two crash days of 1929 registered 12 and 16 million shares respectively, against an average upside volume of around 3 million shares near the bull market top. Thus, it would not surprise me following 1968's average volume of 12 million shares if this market were to produce a downside day or so in the 40 to 50 million share class.

At the turn of the Century, newspaper publisher Peter Dunne created a famous fictional character called Mr. Dooley. Mr. Dooley was quite a philosopher and he was widely quoted. Here's one of his quotes: "No sir, ye can bet it ain't th' people that have no money that causes panics. Panics are th' result iv too many people havin' money. Th' top iv good times is hard times an' th' boom iv hard times is good times. Whin I see a wan man with a shovel on his shoulder dodgin' eight thousand autymobiles, I begin to think 'tis time to put me money in me boot." (with thanks to Ray W. Snyder).

FRENZIED RECORDS: The first hour of trading, Thursday, October 17, broke all records for volume with over 7 million shares being traded (this is two to three times the total daily trading volume of a decade ago).

In August consumer debt jumped $853 million, the biggest rise in the 27-year history of such records.

The third quarter, 1968, announcements of merger intentions rose to a record, fully 64% above the same period a year ago.

Average daily volume for 1968 (estimated) is running at over 12 million shares for the first time in stock exchange history.

OPINION: The London Economist is probably the most sophisticated and reasoned general circulation publication available today. In the latest issue they pose this question: "The decisive question is whether the communists are ready to face a Saigon government that has recovered much of its lost confidence, and is now widening its political support at a time when the communists are much less well placed than they seemed to be in February; in other words, whether they will accept the minority part which is all their following in South Vietnam probably entitles them to, and which is all that President Johnson is prepared to offer them. This may be what Mr. Tho went to Hanoi to decide. The central decision remains, as it always has been, North Vietnam's."

I feel that the Economist states the problem brilliantly. My guess would be that Hanoi will not accept what President Johnson has offered them.

A PLAGUE ON....I was fascinated by this conclusion to an editorial in the current issue of the influential New Republic. It's a highly unusual year when this leading liberal publication refuses to endorse the Democratic candidate. "The old school tie is much in vogue this month, used as a noose around the neck of any liberal who doesn't play the Democratic game: poor sport, bad show. Well, sitting on the sidelines doesn't become a political journal of opinion, and if we could endorse Humphrey (or Nixon) we would. We can't. There are excellent candidates running for a variety of other offices throughout the country. But the only vote we can cast for the top of the ticket is a vote of no confidence."

BEATING FATE: A speculator who has spent many years attempting to beat the market goes to an Indian prophet and is told that one year after his death his estate will increase vastly in value. The speculator posts an obituary notice in the newspaper regarding his own death, then goes into seclusion on a private island. He waits five frustrating years to no avail, the value of his estate actually declines. The speculator dies. A year later three of the estate's largest stock holdings shoot skyward, tripling the value of the estate.

# DOW THEORY MARKET LABORATORY PAGE

In studying charts of all the stocks listed on the N.Y.S.E. (as shown in Quote Digest, 110 N. Lorraine, Wichita, Kans.), I was surprised to see so many triangles forming. The classical triangle is a technical picture of indecision when that triangle is symmetrical. The symmetrical triangle is characterized by the convergence of two trendlines, the upper trendline descending, the lower trendline ascending. The activity within the triangle is usually considered to be "even" buying or selling, literally a struggle between buyers and sellers.

It is generally dangerous to predict the eventual outcome of a symmetrical triangle. Volume implications can be indicative at times. Thus if volume tends to expand on rallies within the triangle, contract on declines, the probability is that the triangle will be resolved to the upside.

More often however, it would pay the student to await the actual breakout of the triangle above or below the trendline. Symmetrical triangles can exert considerable force upon breakouts, and as a rule, the larger the triangle the greater the movement following the ultimate breakout.

I have pictured six outstandingly large triangles which now appear on assorted stocks on the N.Y.S.E. Based on the latest rally, the triangle in Sperry appears rather weak, while the triangle in Monogram Pictures looks as if it wants to break upside.